

# Nova Wellness Group Berhad

**Fair Value: RM0.65**
*Quadruple Capacity by Next Year*
*ACE Market Listing*
**Not Rated**

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## Company Background

Nova Wellness Group Berhad (Nova Wellness) is a nutraceutical company, which is involved in development, production and sales of nutraceutical as well as skincare products under its House Brand and OEM services.

## IPO Structure

Nova Wellness IPO entails issuance of 82.0mn new ordinary shares within the Ace Market of Bursa Malaysia comprising:

- 1) 16.0mn new shares available for the Malaysian public;
- 2) 15.0mn new shares available for application by eligible persons; and
- 3) 51.0mn new shares available by private placement.

Accounting for 25.7% of the enlarged share capital, the IPO price is fixed at RM0.55/share and this will potentially raise total IPO proceeds of RM44.9mn.

## Investment Thesis

- 1) In-house R&D activities;
- 2) Wide distribution network;
- 3) Range of House Brands and OEM;
- 4) Capacity expansion for GMP-compliant facility; and
- 5) Healthy balance sheet.

## Earnings Assumptions

We estimate that the group earnings to increase by an average of 10.9% between FY18 and FY20 considering:

- 1) Management's concerted efforts in widening distribution retail network across Malaysia;
- 2) Commencement of new facility in IQ 2019 after increasing capacity by more than 4x;
- 3) Stable net profit margin at above 40% levels.

## Valuation

We value Nova Wellness at a fair value of **RM0.65**/share based on 13.0x CY19 EPS, which is 30% discount to average peer's PE of 18.0x. **Not rated.**

## Earnings Summary

FYE June (RMmn)	FY16	FY17	FY18E	FY19F	FY20F
Revenue	24.3	24.5	25.7	32.2	41.4
EBITDA	13.9	14.0	14.6	18.6	23.9
EBITDA margin (%)	57.3	57.1	57.0	57.7	57.7
EBIT	13.6	13.6	14.0	17.4	22.1
PBT	13.6	13.6	14.0	17.4	22.0
Net profit	13.5	13.7	11.2	13.9	17.6
Core net profit	13.3	13.2	11.2	13.9	17.6
Core EPS (sen)	4.3	4.3	3.5	4.4	5.6
EPS Growth (%)	10.2	1.3	(18.1)	23.8	26.9
PER (x)	12.9	12.7	15.6	12.6	9.9
DPS (sen)	-	-	1.1	1.3	1.7
Div Yield (sen)	-	-	1.9	2.4	3.0

## Company Background

Nova Wellness is a nutraceutical company which founded in 1989. The group has evolved from trading of animal health products to R&D then develop and produce several nutraceutical products. Principle activities include i) development, production and sales of nutraceutical and skincare products

## Share Information

	Ace Market
Listing	
Enlarged Share Capital (mn)	317.7
Market Cap @ RM0.55 (Rmmn)	174.7
Issue Price (RM)	0.55
Oversubscription Rate	NA
Estimated Free Float (%)	25.7

## Tentative Listing Dates

Opening of the IPO	28-Jun-18
Closing of the IPO	9-Jul-18
Balloting of applications	11-Jul-18
Allotment of shares	19-Jul-18
Listing	20-Jul-18

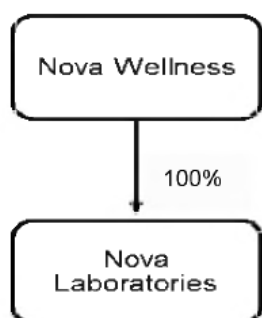
## Ratio and Analysis

NTA per share (post IPO) (RM)	0.1
Price to NTA (x)	3.7
Proforma ROE (%)	58.3
Proforma ROA (%)	31.9
Proforma Gearing (x)	Net Cash

Utilisation of Proceeds	RMmn	%
Construction of new facility	16.5	36.7
Research and development	11.6	25.8
Retail market expansion	5.0	11.2
Working capital	9.2	20.5
Listing Expenses	2.6	5.8
<b>Total</b>	<b>44.9</b>	<b>100.0</b>

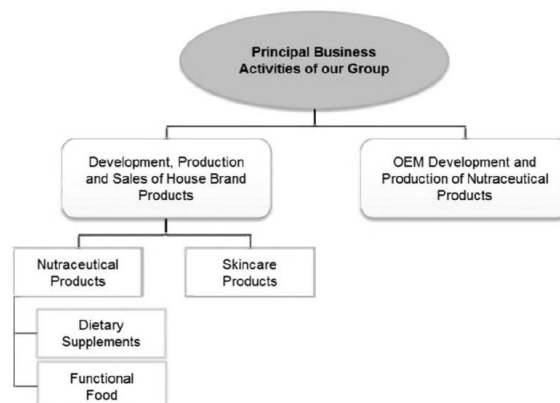
under its House Brands; as well as ii) OEM development and production of nutraceutical products.

**Figure 1 : Group Structure**



Source: Company, TA Securities

**Figure 2 : Business Activities**

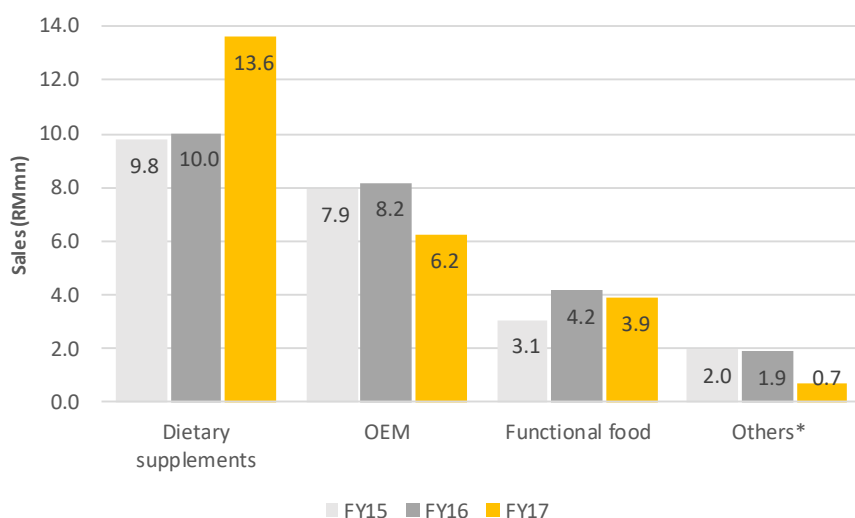


Source: Company, TA Securities

Nova Wellness has developed 144 product formulations with 80 products sold locally and abroad under House Brands; i.e.: i) Nova; ii) ActivMax; iii) Sustinex; iv) Novavis and; v) SP8. While under the OEM segment, the group has developed 88 products formulations with 74 products manufactured for OEM customers under brands like i) Powerlife; ii) Eastern; iii) ActiveLife; iv) HSC; v) Nexus; vi) COCO.LAB and; vii) BELVEA.

In FY17, Nova Wellness achieved sales of RM24.5mn. which was less than 1% increase YoY. This was due to increased contribution from dietary supplements products by 35.8% YoY, which offset by lower earnings from OEM, Functional Food and Others by 23.5%, 6.2% and 62.5% YoY respectively. Note that Nova Wellness has discontinued selling animal health products within the Others segment since January 2017, which caused the sales decline in the segment. See Figure 3 below.

**Figure 3 : Sales Breakdown Over the Years**



Source: Company, TA Securities

\* Animal health products which were discontinued since Jan 2017.

### Key Management and Substantial Shareholders

The founders of Nova Wellness are husband and wife Phang Nyie Lin and Tan Sok Mooi whom will be the substantial shareholders and promoters where each will be holding 5.1% and 53.9% respectively post IPO. Nyie Lin is also an executive director with the role of managing director and chief research officer of the group. While Sok Mooi is the director of the group holding the title of chief human resources officer.

The couple has three sons who are also promoters, substantial shareholders as well as executive directors of the company. Their roles include business development manager, marketing as well as R&D product formulation, and purchasing officer. The family is heavily involved in running the company with close to 30 years work experience in the industry.

**Figure 4 : Substantial Shareholders and Promoters**

Name	Before IPO		Post IPO (1st Moratorium)		Post IPO (2nd Moratorium)	
	mn shares	%	mn shares	%	mn shares	%
Phang Nyie Lin	16.2	6.8	16.2	5.1	15.3	4.8
Tan Sok Mooi	171.8	72.8	171.8	53.9	81.8	25.8
Phang Yeen Nung	16.2	6.8	16.2	5.1	15.3	4.8
Phang Yeen Aun	16.2	6.8	16.2	5.1	15.3	4.8
Phang Yeen Hung	16.2	6.8	16.2	5.1	15.3	4.8
<b>Total</b>	<b>236.4</b>	<b>100.0</b>	<b>236.4</b>	<b>74.3</b>	<b>143.0</b>	<b>45.0</b>

Source: Company, TA Securities

Note that after the IPO, Nova Wellness other key management are also expected to directly hold 0.09% each of the group's holding, including:

- 1) Yeoh Kim Kooi (CFO);
- 2) Nicholas Cheong Peck Hiang (Chief Business Officer);
- 3) Tan Kiat Wei (Chief Production Officer); and
- 4) Sangheeta A/P Thuraisingam (Chief Quality Officer).

### Utilisation of Proceeds

The group is estimated to raise RM44.9mn which is expected to be utilised in the following manners:

**Figure 5 : Use of Proceeds**

Descriptions	Amount (RMmn)	Breakdown of Proceeds (%)	Est. Utilisation Timeframe
Construction of new GMP-compliant production capacity	16.5	36.6	24 months
R&D activities	11.6	25.7	36 months
Expansion of retail market presence	5.0	11.1	36 months
Working capital	9.2	20.8	12 months
Estimated listing expense	2.6	5.8	Immediate
<b>Total Gross Proceeds</b>	<b>44.9</b>	<b>100.0</b>	

Source: Company, TA Securities

### Investment Thesis

#### 1) In-House R&D Activities

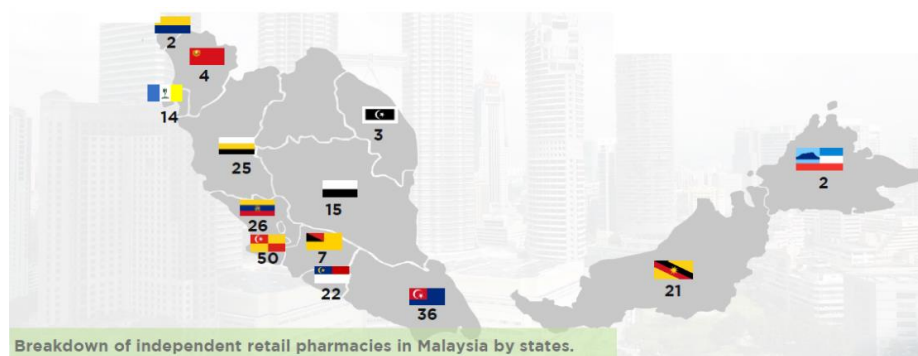
Nova Wellness's R&D expenditure totalled to RM0.89mn between FY15 to FY17 for pre-clinical and clinical trials on nutraceuticals and skincare products. Moving forward, Nova Wellness plans to utilise RM11.6mn of the IPO proceeds together with grant awarded from NKEA Agricultural Scheme for the following; i) second and third clinical trial for Hepar-P Capsule used for liver protection agent; ii) clinical trials on Ficus Cream products for skin lightening; iii) pre-clinical and clinical trials on a nutraceutical product containing oil palm

leaves standardised extract; and iv) other ingredients developments for food colourants and snacks. These R&D are expected to complete by end-2020.

### 2) Wide Distribution Network

As seen on Figure 6 below, Nova Wellness has distribution network nationwide in Malaysia. Nova Wellness' products are found in 227 independent retail pharmacies where 105 are registered with the Nova Wellness Partnership Programme (NWPP). The NWPP signed a contract with Nova Wellness to purchase monthly commitment which provide consistent sales to the group. Post IPO, Nova Wellness plans to utilise RM5.0mn of IPO proceeds to expand its presence in the retail market by acquiring 41 and 51 new NWPP in 2018 and 2019 respectively. Note that domestic sales account for 95% of the group's revenue.

**Figure 6 : Nationwide Distribution Network**



Source: Company, TA Securities

### 3) Range of House Brands and OEM

Nova Wellness has 49 dietary supplements, 11 functional products and 28 skincare products sold under the House Brands. Products are sold locally and domestically. Moreover, the group manufactures 72 dietary supplements and two functional food products for OEM services. Following the completion of R&D activities post-IPO, Nova Wellness can formulate new products to further expand its product portfolio while meeting market demands. Note that according to Institute of Medical Research, Nova Wellness account for 1.5% of the Malaysian nutraceutical market in 2017.

**Figure 7 : Nova Wellness House Brands Product Range**



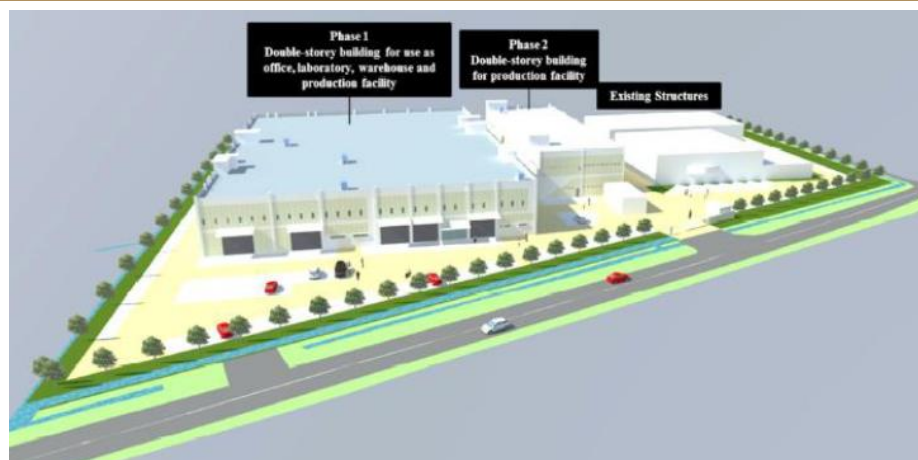
Source: Company, TA Securities

### 4) Capacity Expansion

Nova Wellness plant is in Sepang, Selangor, which currently used for R&D and production of dietary product range with capacity of 0.7mn bottles and sachets. By 1Q 2019, Nova Wellness hopes to more than quadruple production capacity to 3.4mn sachets and bottles. Construction will be in two phases

where 1<sup>st</sup> phase is a double-storey building for operations of functional food products as well as warehouse for all product range. The 2<sup>nd</sup> phase building will be used for skincare products operations. Management guided that RM16.5mn of the IPO proceeds will be used for this project.

**Figure 8 : New GMP-Compliant Facility**



Source: Company, TA Securities

### 5) *Healthy Balance Sheet*

For FY18, the group suggests a dividend policy of 30% payout from net earnings. Moving forward, dividend payout will be determined by the group's future earnings. Note that Nova Wellness has no borrowings with net cash position. As such, we do not foresee issue in delivering the dividend policy for FY18 due to the healthy balance sheet.

## *Risks*

### 1) *Highly Competitive Landscape*

According to Protégé Associates (market research and business consulting company), there are approximately 5,000 players in Malaysia which are involved in the manufacturing and/or importing nutraceutical products. Within the dietary supplements range which commands market value of RM1.3bn in 2017, Nova Wellness holds less than 1.0% of the market share in Malaysia. Players tend to compete in terms of pricing therefore price elasticity of demand of nutraceutical products are highly elastic.

### 2) *Taxation Costs*

In the past 10 years, Nova Wellness was eligible for a 100% tax exemption due to its BioNexus-status by Malaysian Bioeconomy Development in 2006. Upon expiry in FY17, Nova Wellness is eligible to a concessionary tax rate of 20% on statutory income generated from its qualifying activities for another period of 10 years. Management guided that the group has submitted the application for the concessionary tax rate and currently pending approval. Without the approval, Nova Wellness is subject to the normal corporate tax rate of 24% in 2018 which is expected to reduce the group's net earnings margins in the future.

### 3) *Fluctuation in Foreign Exchange Rate*

About 6.6% of the group's cost of sales comprises import of packaging and raw materials from overseas, where payments are made in RMB and USD. While the export sales are mainly denominated in USD which account for 5.4% of the group's total sales. This mismatch of import and export would expose the

company to foreign exchange rate fluctuations. Note that weakening of Ringgit is expected to benefit Nova Wellness more as degree of export sales is higher than the degree of imported costs.

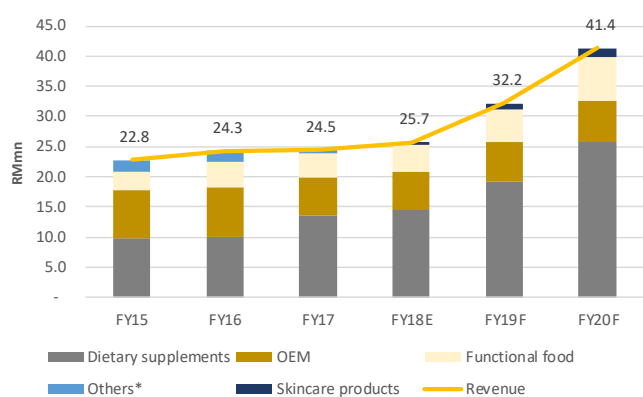
### Financial Review

FY16 earnings grew by 10.2% YoY to RM13.5mn due to positive sales contributions. Revenue increased by 7.9% YoY to RM24.3mn on the back of increase in domestic sales (+2.0% YoY) within the House Brands and OEM range as well as export sales (+47.4% YoY) from the OEM segment and animal health segment products.

For FY17, the group recorded a revenue of RM24.5mn (+1.1% YoY) due to increase in domestic sales (+12.1% YoY) which offset by decline in export sales (-38.0% YoY). Hence net profit was relatively flat at RM13.7mn (+1.3% YoY) as net margin improved due to decrease in costs of sales within the OEM segment.

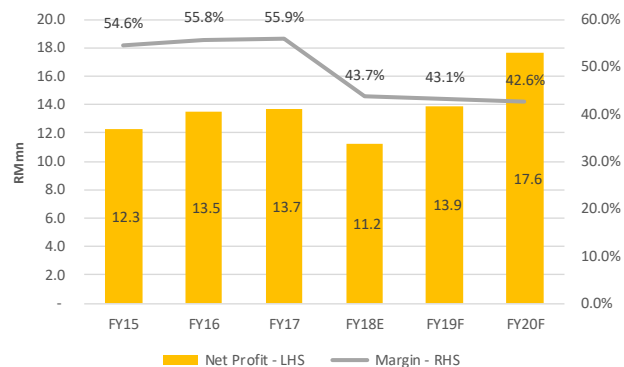
Note that the group had BioNexus-status. Hence, was eligible for 100% tax exemption for the past 10 years until end of FY17. Moving forward, we project that Nova Wellness will incur a 20% corporate tax rate thereby reducing the FY18 net profit by 18.1% YoY to RM11.2mn. However, given the expansion plans, which include i) more R&D activities to develop clinically tested products; ii) capacity expansion of GMP-compliant facility; as well as iii) management efforts in expanding retail distributions, we believe that Nova Wellness to experience double digit growth in earnings for FY19 and FY20 at 23.8% and 26.9% respectively.

Figure 9 : Revenue Breakdown



Source: Company, TA Securities

Figure 10 : Net Profit and Margin



Source: Company, TA Securities

### Valuation

At the IPO price of RM0.55/share, Nova Wellness is priced at FY17 PE of 12.8x. We value Nova Wellness at a fair value of **RM0.65**/share based on 13.0x CY19 EPS, which is about 30% discount to its peer's average PE of 18.0x. The discount is given due to the highly competitively nature of the business and the smaller production capacity as compared to its closest peers.

**Table 1: Earnings Summary (RMmn)**

FYE June (RMmn)	FY16	FY17	FY18E	FY19F	FY20F
Revenue	24.3	24.5	25.7	32.2	41.4
EBITDA	13.9	14.0	14.6	18.6	23.9
EBITDA margin (%)	57.3	57.1	57.0	57.7	57.7
EBIT	13.6	13.6	14.0	17.4	22.1
PBT	13.6	13.6	14.0	17.4	22.0
Net profit	13.5	13.7	11.2	13.9	17.6
Core net profit	13.3	13.2	11.2	13.9	17.6
Core EPS (sen)	4.3	4.3	3.5	4.4	5.6
EPS Growth (%)	10.2	1.3	(18.1)	23.8	26.9
PER (x)	12.9	12.7	15.6	12.6	9.9
DPS (sen)	-	-	1.1	1.3	1.7
Div Yield (sen)	-	-	1.9	2.4	3.0

**Table 2: Peers Comparison**

Companies	Share Price (RM)	Market Cap (RMmn)	PER (x)		EPS Growth (%)		Dividend Yield (%)	
			2018	2019	2018	2019	2018	2019
Amway	7.53	1,237.8	21.1	20.1	11.3	5.2	4.6	4.9
Hai-O	4.80	1,396.5	15.0	13.1	22.5	14.4	3.8	4.7
Power Root	1.79	579.3	17.1	12.7	19.0	34.8	5.5	6.3
<b>Simple Average</b>		<b>1,071.2</b>	<b>17.7</b>	<b>15.3</b>	<b>17.6</b>	<b>18.1</b>	<b>4.6</b>	<b>5.3</b>
Nova Wellness	0.55	174.7	14.1	11.2	2.8	25.3	2.2	2.7

### Stock Recommendation Guideline

- BUY** : Total return within the next 12 months exceeds required rate of return by 5%-point.  
**HOLD** : Total return within the next 12 months exceeds required rate of return by between 0-5%-point.  
**SELL** : Total return is lower than the required rate of return.  
**Not Rated**: The company is not under coverage. The report is for information only.

**Total Return** is defined as expected share price appreciation plus gross dividend over the next 12 months. Gross dividend is excluded from total return if dividend discount model valuation is used to avoid double counting.

**Required Rate of Return** of 7% is defined as the yield for one-year Malaysian government treasury plus assumed equity risk premium.

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As of Wednesday, July 04, 2018, the analyst, Damia Othman, who prepared this report, has interest in the following securities covered in this report:  
(a) nil

**Kaladher Govindan – Head of Research**

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